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TAGS: ECON ETRD EINV EAGR NU
SUBJECT: NICARAGUA: ECONOMIC OUTLOOK BLEAK FOR 2009

REF: A. MANAGUA 0133
¶B. MANAGUA 0116

Classified By: Ambassador Robert J. Callahan, reasons 1.4 (b) and (d).

Summary

¶1. (C) Businessmen and economists gathered for the Ambassador's May 15 roundtable focused their discussion on the global economic crisis, the Nicaraguan political crisis, and deficit financing. One local economist predicted that the economy would contract by 1%. A banking executive noted that failure to secure budget support from the International Monetary Fund (IMF) or other international donors could result in capital flight and currency devaluation. Business owners reported falling sales as a result of a decrease in overall demand. Roundtable participants stressed the gravity of a growing credit crunch on the supply side. Manufacturers and farmers are suffering from a lack of financing. End summary.

Economic Contraction of 1% Forecast for 2009

¶2. (C) On May 15, the Ambassador hosted a group of prominent local businessmen and economists for a roundtable discussion on the economy. Mario Arana, Executive Director of the Foundation for Economic and Social Development (FUNIDES), opened the discussion with a macroeconomic overview. FUNIDES estimates that the Nicaraguan economy will contract in 2009 by 1% or more. Arana noted that this scenario is more pessimistic than the IMF's projection of 0.5% growth for the year. The GON continues to project 2% growth, but this seems out of the realm of possibility.

Economic Stability Threatened by Budget Gap

¶3. (C) Further discussion of the macroeconomy focused on how the government would finance its budget deficit, now estimated to be $150 million for 2009. Arana argued that the next few weeks would be crucial, as the government negotiates with the IMF over revisions to its program. Government officials have indicated that the Finance Ministry would soon place $80 million in bonds on the local market, but Luis Rivas of BANPRO, Nicaragua's largest bank, doubts that there is that much appetite for government paper right now. Rivas agreed with Arana that the GON needs international donors to provide budget support. Donors, however, continue to withhold funds as long as the government refuses to address fraudulent municipal elections held in November 2008. The government appears to be hoping that its close ally Venezuela will come through at the last minute.

¶4. (C) Arana spent some time describing the pessimistic scenario in which the government loses its IMF program and donors refuse to close the budget deficit. If the government fails to finance its deficit with bonds purchased by local banks or Venezuelan entities, it would be forced to withdraw funds from its reserves. Arana argued that financing the budget deficit with foreign reserves would trigger a run on the banks and a possible economic meltdown. So far, however, capital flight has not been a serious problem.

Sales Down for Many Businesses

¶5. (C) Moving from the macroeconomic to the microeconomic view, a representative from the only textile mill in Nicaragua, Cone Denim (part of the International Textile Group based in North Carolina), explained that the company closed its $100 million denim mill in response to a steep drop in demand. The company wants to reopen the plant as soon as possible, but it may be a year before it happens.

¶6. (C) Mario Salvo, owner of dairy company El Eskimo, reported that ice cream sales are down by 13% this year as compared to 2008. In response, his company is introducing less expensive products with lower profit margins in an attempt to retain its predominant market share. On the positive side, Roberto Bendana of Don Paco Coffee noted that while Nicaragua's coffee production was down 30% during the 2008-2009 harvest, the outlook for 2010 is positive. Producers are forecasting a better harvest, and international prices have improved.

¶7. (C) Ricardo Teran, who distributes Kodak and Hewlett Packard equipment, among other U.S. consumer products, reported that many businesses have decreased capital investment. He also reported that sales are down at Managua's large shopping centers. Moreover, from January to March 2009, imports fell 60% when compared to the same period in 2008. Teran believes that part of this decrease can be attributed to the Nicaraguan Customs Agency's (DGA) decision to abandon selective inspection for 100% inspection of all imports. Custom delays increase shipping costs, making imported goods costlier.

Credit Crunch Affecting Supply Side

¶8. (C) Besides the effect that weak international demand is having on local economic activity, roundtable participants stressed the gravity of the growing credit crunch on the supply side. According to Luis Rivas, international banks have cut lines of credit to local banks and suspended most direct lending to local manufacturers. To retain liquidity, Nicaraguan banks have decreased local lending, particularly to exporters and agricultural producers. Lines of credit to importers have fallen by 40%, Rivas reported, and loan periods sometimes have been cut in half. Without adequate financing, many manufacturers and farmers are suffering.

¶9. (C) Duilio Baltodano, President of agricultural wholesaler Cisa Agro, pointed out that fertilizer sales are down at the same time Nicaraguan farmers are planting crops. Without financing for fertilizer and other inputs, yields will be low, making it even more difficult for farmers to repay existing debts. This could be the beginning of a vicious downward spiral.

¶10. (C) Rivas added that even when funds are available for agriculture -- for cattle, for example -- local banks are not lending out of fear that the &No Payment8 movement will inspire borrowers to default on their loans (Ref B). While the delinquency rate on cattle loans is historically 1%, the &No Payment8 movement has caused it to climb to 7%.

Comment

¶11. (C) Nicaragua suffers from a lack of finance, both public

and private, as a result of the international economic crisis and the politics of the Ortega administration. Through new financing facilities for developing countries, the IMF is likely to provide some percentage of the $150 million needed to finance the 2009 budget deficit. Should Venezuelan funding fail to materialize as many predict, the government is likely to go through with plans to sell bonds, perhaps forcing local banks to buy them or using proceeds from its oil import scheme with Venezuela to buy them. Forcing local banks to participate may only exacerbate the already crippling credit crunch.
CALLAHAN